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ABSTRACT

This speech concentrates on a discussion of the increasing difficulty that school districts are experiencing in obtaining insurance coverage. The speaker offers school administrators some suggestions to assist them in securing the necessary coverage and suggests that when an insurance market is open and competitive, purchasing through bidding is appropriate. However, he cautions that, in a tight market, negotiation with insurance companies through a professionally competent insurance broker is more desirable. (JF)

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"CHANGES IN PURCHASING PRACTICES OF SCHOOL INSURANCE - - OR, TO BID OR NOT TO BID."

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by

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CHANGES IN PURCHASING PRACTICES OF SCHOOL INSURANCE --
OR, TO BID OR NOT TO BID.

It is no longer necessary to dwell on the fact that school districts are having difficulty in acquiring certain kinds of insurance. Almost without exception, however, every school district throughout this nation has been able to buy insurance coverage of some form to, at least, partially insure their risks. However, if we make any kind of study wherein we compare problems of acquisition and costs of insurance today with the problems of acquisition and costs of insurance as early as three years ago, we must accept the fact conditions have taken a drastic change. Those things we were doing five, and even three years ago, may not produce desired results today.

Don Burch, Risk Management Administrator for the Pinellas County, Florida, School Board, made this statement as an introduction to his recent article "Risk Management For School Districts" for the Croft School Business Service Report for August, 1971 --

> "Insurance Companies are becoming more and more reluctant to write insurance for schools, and are subjecting all lines of school insurance to stringent scrutiny. In Pinellas County, we recently went through the gymnastics of purchasing fire and extended coverage -- with traumatic financial results. Our premium cost increased almost four times, and our coverage was so reduced that it was necessary to self-insure a great portion of our risk."
>
> "It is obvious that school administrators can no longer afford to treat insurance as a traditional item to be purchased -- and

then forgotten until a loss takes place. They must review their insurance programs in the light of dollar cost in the school budget. They must develop methods of buying realistic protection for realistic reasons".

There are many school districts that have had this same traumatic experience in recent months. Many more districts will have similar experiences in the months to come.

Just a few short years ago school insurance was premium business, earnestly sought after by insurance companies with the offer of extremely low rates resulting in a minimum effect on the school budget. Under these conditions many school business managers developed the feeling insurance is something that must be purchased, maybe because the law required it, or because it just made good sense to do so -- that it was a necessary evil, like taxes. Under these conditions three general circumstances developed:

1) the school districts insurance program was a political element of the school district's operation and the Board of Education found it politically expedient to turn the District's insurance program over to an association of insurance agents and/or brokers for it to administer. Under these conditions, many times, no one individual had complete responsibility for the program and a good portion of the time there was little concern as to what could be done to keep the cost of the program to a minimum while still providing the most comprehensive insurance coverage consistent with the District's needs.

2) A comparable condition developed when the Board of Education took the position, and rightly so, that insurance is a

highly specialized field and assigned the insurance program to a specific individual agent, with almost complete authority to write the insurance programs of the District as he and the Board of Education could agree they should be written, and the chief school administrator, and particularly, the chief school business official had little or nothing to say about the administration of the program and its attendant cost.

3) A third condition developed when it was realized that school insurance could be purchased on a highly competitive market with many underwriters considering school district property and liability insurance as premium business. A part of the market in which rates established by the rating bureaus could be completely ignored and sizeable discounts extended in order to secure the business. Under these conditions, many school districts became complacent about their insurance programs. They took the position that this "necessary evil" should be purchased with the strictest of specifications prepared under the philosophy that all responsibility for loss should be transferred to the insurance company -- that competitive bids should be taken from as many companies as possible with the business awarded to the company, or companies, offering the lowest premium rate. Many times, in this climate of highly competitive business, school districts found it to their financial interests to cancel policies before expiration and re-bid because of adjustments in the market, thus resulting in the insurance program being passed along from one company to another in relatively short periods of time.

It is not for me to say that under any of these general situations that the best interests of the school districts were not properly served in most situations. You and I know that there are insurance associations and individual agents that have rendered extremely fine service and, many times, without profit to themselves on the school district business. Also, we know that a great number of districts have been adequately and properly served by insurance companies under the conditions of a highly competitive market for school district insurance.

But the climate and conditions under which school districts operate today demand that the whole business of school district insurance be administered in an atmosphere in which the district's needs are clearly defined after determining what the district can do to make its insurance program more attractive. Once this determination is made, a program of insurance, designed to fit those needs, is obtained at the minimum cost possible.

This discussion focuses on the question -- "To Bid or Not To Bid". There might be conditions under which some chief school business officials believe that after they have taken the necessary steps to make their district's program attractive to several companies that bidding is the most feasible method for them to obtain the insurance needed. In view of all the circumstances, I have reviewed, it is my position that formal bidding, as we have known it in the past, is <u>not</u> the way to obtain the district's property and liability insurance.

Let me quote to you from a letter I recently received from one of the Vice Presidents of the Continental Insurance Companies in response to the question "Should school district's bid its property insurance programs?" --

" . . . . insurance company representatives . . . . (have) made it clear that it was highly preferred that the buyer and his broker negotiate rather than bid. If invitations to bid are prepared and distributed to a number of companies, particularly on a classification that at the time is not considered attractive, the company underwriters may say to themselves, 'Why should we bid for business we are not seeking.'

"There is also a great deal of work involved by all parties in preparing bid proposals. The underwriter has to weigh the cost of preparing the bid and his chances of getting the business. His decision not to bid could easily be based on the cost of preparing the bid.

> "Generally, I believe bidding for certain items is probably a healthly form of competition, but insurance is not necessarily that kind of commodity. Insurance on schools and political subdivisions should be based on a long pull situation rather than an in and out bid set-up where the carrier is not certain they will have the business from one year to the next."

Though some might take exception to the general statement that insurance is not necessarily a commodity that should be purchased through bidding, we can hardly ignore the question, "Why should we bid for business we are not seeking?"

However, the most important factor affecting your answer to the question, "Should you distribute insurance specifications for competitive bidding?" is the insurance market. If the market for your class of operation is open and generally competitive, the answer should normally be in the

affirmative. On the other hand, if it is the reverse, negotiation with one or more brokers may be a better answer.

Should the market for your class of business be competitive and you determine your district can best be served by competitive bidding, there are two points to consider when preparing and distributing specifications:

1) Specifications should be prepared by someone both professionally competent and objective -- you might even wish to consider someone not associated with an insurance company or producer.
2) Distribution of the specifications should be limited to a number of qualified agents, brokers and direct-writing companies. If the specifications are too broadly distributed, the result could be a dilution of the market causing some of the better potential bidders to bid high or refuse to bid at all.

Also, if your district is committed to competitive bidding, the frequency of bidding is important. If you invite outside bids every renewal, such as every three years, it is likely that quotations received will not be as low as otherwise might be expected, or that some sources will not bid at all. Underwriters need a reasonable amount of time to cushion bad years with good ones. Competitive bidding on a less infrequest basis is a recommended balance.

However, many districts have experienced the same traumatic experience referred to earlier by adhering to the principle of acquiring school district insurance through competitive bidding. Many of these districts are now learning that their best insurance program at the least cost is obtained by:

1) determing the district's insurance needs. This should be done in cooperation with a competent broker or an independent professional insurance counselor.

2) Selection of an experienced, professionally competent insurance broker.

3) Assumption of a portion of the risk by the school district, within financial limitations of the district and legal requirements, if applicable.

4) A sound program of risk management, clearly supported by school district policy, communicated in detail to probable underwriters.

5) Negotiation with one or more qualified companies as the district's broker feels necessary to obtain the lowest premium cost consistent with the district's insurance program needs.

It can be stated unqualifiedly that of the points listed the most important one is the selection of a professionally competent insurance broker. A few years ago Richard A. Archer, President of Allen T. Archer Co., spoke to the California Association of School Business Officials on the topic "Guidelines for Selection of A Competent Insurance Broker". Among the attributes of a competent broker he listed the following:

1) Availability to a broad segment of the insurance market.
   a) No single company can possibly and consistently meet the complete needs of an insured.
   b) Have a variety of programs available.
   c) Capacity to develop competive premium terms.
   d) Capacity to solve high value problems.

2) A competent staff is necessary for service in depth.

   a) School districts, large and small, have need for numerous types of insurance, many of which are complicated and require specialized knowledge.

   b) Insurance is business of people and their competency in large measure determines the quality of a district's insurance program.

3) Character is an important attribute.

   a) The broker's business should have an established reputation for fair dealings and high ethical standards.

   b) The principals of the firm should be favorably regarded and respected in the community and within their industry.

When the Board of Education appoints an insurance broker to handle the insurance program of the school district, they are entrusting the protection of all of the District's assets to him. The soundness and integrity of this individual or firm can spell the difference between preservation or loss of assets.

Taking the matter of the broker one step farther "What should the school district expect of its broker?", Mr. Archer says, we should at least expect the following:

1) Continued survey and analysis of insurable exposures and continually informing the district's administration of these exposures.

2) Work out programs in cooperation with district administration and insurance counselor, when deemed necessary, for insuring those exposures which the insured wishes covered by insurance.

3) Submit for marketing and negotiation developed specifications to a cross section of the insurance market. Among many things, selection of a carrier should include financial integrity and loss paying reputation as well as the reputation the carrier has for staying with placement and not indiscriminately cancelling.

4) Periodic inspection of properties to verify property values and substantiate fire rating and casualty insurance classifications. As a part of his continuing service, the broker should offer the district assistance with periodic safety inspections and safety engineering programs.

5) In the case of a loss, a competent broker should immediately arrange for an adjuster, personally inspect larger losses, assist in preparation of loss reports, assist in loss negotiations and make every effort to see that payment of claim is expedited.

The only time one can evaluate the worth of insurance is at the time of a loss. Most insureds are not accustomed to having losses and thus broker representation is essential for the insured to obtain a fair and prompt settlement.

Some risks managers claim to be able to operate effectively without a broker. Such a belief apparently considers the broker as some sort of middle man who get between them (the risk manager) and the source of protection. This atitude overlooks the chief value of a good broker which is the knowledge of markets and the methods best suited to their development.

School districts today know that insurance underwriters can be both fickle and prejudiced, in the literal rather than the derogatory sense. They are fickle because they readily write a policy of insurance and as quickly cancel or refuse to renew. They are prejudiced because of conditioning with certain types of risks. These individual and human characteristics make it imperitive to have a broker who is knowledgeable with regard to the peculiarities of each market as well as the techniques by which a particular piece of business can be presented to best advantage. The method by which an offering is presented to an underwriter can play a large part in its acceptance or rejection and rating.

In recent years, we have heard the term "risk management" used as the proper term in substitution for "administration of an insurance program". Recently our own committee has been designated "Risk Management Research Committee" instead of "Insurance Research Committee". The comprehensive concept of risk management is highly recommended for adoption by every school district. Time will permit mentioning only the basic principles of risk management, which are" risk identification, risk prevention and control, risk assumption by the district, the sharing of risks and the transferring of risks. The application of these sound risk principles and the use of an effective competent insurance broker will not completely solve all of your school district insurance problems. However, since school district insurance can no longer be considered a "cut and dried" matter; and since it is important for school district to talk to insurance companies about conditions within the district, about measures being taken to reduce risk; and since the services of a good broker completely aware of conditions within the district is essential; and, since the introduction of the risk management concept to school insurance is not compatible

with formal bidding procedures; it is apparent that changes in purchasing practices of school insurance are occuring and perhaps there is no longer a question of "To Bid or Not To Bid?"